Report

of the

Examination of

Spring Grove Mutual Insurance Company

Brodhead, Wisconsin

As of December 31, 2002

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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July 11, 2003

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2002, of the affairs and financial condition of

SPRING GROVE MUTUAL INSURANCE COMPANY
Brodhead, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The last examination of Spring Grove Mutual Insurance Company (hereinafter also "the company"), was made in 1998 as of December 31, 1997. The current examination covered the intervening time period ending December 31, 2002, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on January 5, 1875, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Mutual Fire Insurance Company of the Town of Spring Grove, Decatur, and Albany. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there was one amendment to the articles of incorporation and no amendment to the bylaws. The articles of incorporation were amended to increase the company's authorized territory to include Lafayette County.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Dane, Green, Rock, Walworth, and Lafayette

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance.

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements for terms of one year with premiums payable on the advance premium basis. Policy fees charged to policyholders are retained by the company.

Business of the company is acquired through three agents, two of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
Property	New Business 15% Renewals 10%

Agents have authority to adjust losses up to $500.00. Losses in excess of this amount are adjusted by the Adjusting Committee. Adjusters receive $25.00 for each loss adjusted plus $.32 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of seven members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
James Beutel*	Farmer/Agent	Brodhead, WI	2004
Joyce Binder	Farmer	Monticello, WI	2004
Roger Brugger	Farmer	Monticello, WI	2005
Geraldine Lee*	Tax Preparer/Farmer	Brodhead, WI	2005
Nick Faessler	Farmer	Brodhead, WI	2006
Virgil Meinert	Retired	Brodhead, WI	2006
Thomas Ten Eyck	Farmer	Brodhead, WI	2006

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $35.00 for each meeting attended and $.32 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

Name	Office	2002 Salary
James Beutel	President	$1,000
Joyce Binder	Vice President	300
Geraldine Lee	Secretary/Treasurer	5,000

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee
James Beutel, Chair
Joyce Binder
Roger Brugger
Nick Faessler
Geraldine Lee
Virgil Meinert
Thomas Ten Eyck

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Net Losses and LAE Incurred	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2002	$76,507	$106,971	392	$(55,796)	$1,315,781	$1,224,476
2001	75,893	36,633	393	28,826	1,408,403	1,327,543
2000	85,414	51,915	386	20,201	1,408,382	1,306,212
1999	91,085	108,075	410	(36,733)	1,359,682	1,268,534
1998	84,204	42,782	411	18,215	1,403,665	1,310,464

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Gross	Writings Ratios Net
2002	$226,051	$82,230	$1,224,476	18%	7%
2001	213,942	75,187	1,327,543	16	6
2000	211,755	83,999	1,306,212	16	6
1998	206,186	87,009	1,310,464	16	7
1999	209,867	91,419	1,268,534	17	7

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
2002	$106,971	$76,597	$76,507	140%	100%	240%
2001	36,633	72,409	75,893	48	95	143
2000	51,915	76,546	85,414	61	90	161
1999	108,075	90,978	91,085	119	100	219
1998	42,782	84,641	84,204	51	101	152

The company experienced its greatest losses in the prior five year period in 2002, including four major house fires and one barn fire. Surplus has decreased 6% from 1998 primarily due to the unfavorable loss experiences in 2002. The company has experienced a fluctuating loss ratio, while the expense ratio remains relatively high primarily due to the company’s small premium volume. Despite the poor results in terms of the expenses, and to a lesser extent losses, the company continues to have adequate surplus due to its low premium to surplus ratio.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2003
Termination provisions:	Either the company or the reinsurer may terminate the contract and/or any of the attached exhibits as of January 1, 2004, or any subsequent January 1, by giving to the other party at least 90 days advance notice in writing.

The coverage provided under this treaty is summarized as follows:

1.	Type of contract:	Class A - Casualty Quota Share Reinsurance
	Lines reinsured:	All business classified as casualty business.
	Company's retention:	The company shall cede on a pro rata basis and the Reinsurer shall assume 100% of the company's business.
	Coverage:	100% of each and every loss occurring on the business covered by this contract, including loss adjustment expenses. Coverage is subject to maximum policy limits of $1,000,000 per occurrence, in any combination of bodily injury and property damage liability; $5,000 for medical payments per person, $25,000 per accident.
	Reinsurance premium:	100% of the unearned premiums applicable to business covered by this exhibit.
	Commission:	15%
2.	Type of contract:	Class B First Surplus Reinsurance
	Lines reinsured:	All property business written by the company.
	Company's retention:	$150,000 per ceded risk or at least 50% on a pro rata basis per ceded risk when the company's net retention is $150,000 or less in respect to a risk. Additionally, the company retains an annual aggregate deductible equal to 10% of the loss and loss adjustment expenses otherwise recoverable.
	Coverage:	Up to $800,000 on a pro rata basis when the company's net retention is $150,000 or more in respect to a risk. When the company's net retention is $150,000 or less in respect to a risk, the company may cede on a pro rata basis up to 50% of such risk.

	Reinsurance Premium:	Pro rata share of all premiums and fees charged by the company corresponding to the amount of each risk ceded.
	Ceding Commission:	15% to 35%, depending on loss experience.
3.	Type of contract:	Class C-1 Excess of Loss - First Layer
	Lines reinsured:	All property business written by the company.
	Company's retention:	\$30,000 per occurrence \$30,000 annual aggregate deductible
	Coverage:	100% of any loss, including loss adjustment expense, in excess of \$30,000, subject to a limit of liability to the reinsurer of \$70,000.
	Reinsurance Premium:	Based on experience over the past four years with load factor of 125%. Minimum rate: 6% of current net premiums written Maximum rate: 19% of current net premiums written Current rate: 6% Premium deposit: \$7,200 Minimum premium of \$5,800
4.	Type of contract:	Class C-2 Excess of Loss - Second Layer (Flat rated)
	Lines reinsured:	All property business written by the company.
	Company's retention:	\$100,000
	Coverage:	100% of any loss, including loss adjustment expense, in excess of \$100,000, subject to a limit of liability to the reinsurer of \$50,000.
	Reinsurance premium:	6% of the company's current net premiums written in respect to the business covered. Premium deposit: \$7,200 Minimum premium of \$5,800
5.	Type of contract:	Class D/E Stop Loss Reinsurance
	Lines reinsured:	All business written by the company.
	Company's Retention:	75% of net written premium.
	Coverage:	100% of the amount by which the aggregate of the company's losses, including loss adjustment expenses exceed the retention.
	Reinsurance premium:	Current rate based on a formula calculation which takes into account the losses incurred by the reinsurer under this contract for the last eight years. Minimum rate: 6% of the current net written premiums. Maximum rate: 25% of the current net written premiums. Current rate: 14.83%. Premium deposit: \$17,700 Minimum premium of \$14,500

III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement at December 31, 2002. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Spring Grove Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2002

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in Company's Office	$50			$50
Cash Deposited in Checking Account	12,987			12,987
Cash Deposited at Interest	358,018			358,018
Bonds (at Amortized Cost)	271,536			271,536
Stocks or Mutual Fund Investments (at Market)	379,443			379,443
Mortgage Loans on Real Estate				
Real Estate	76,051			76,051
Notes Receivable				
Premiums and Agents' Balances and Installments:				
In Course of Collection	1,802			1,802
Deferred and Not Yet Due	15,144			15,144
Investment Income Accrued		$4,530		4,530
Reinsurance Recoverable on Paid Losses and LAE	189,319			189,319
Electronic Data Processing Equipment	6,901			6,901
Furniture and Fixtures			$773	0
TOTALS	$1,311,251	$4,530	$773	$1,315,781

Spring Grove Mutual Insurance Company
Statement of Assets and Liabilities (cont.)
As of December 31, 2002

Liabilities and Surplus

Net Unpaid Losses	$12,387
Unpaid Loss Adjustment Expenses	500
Commissions Payable	1,695
Fire Department Dues Payable	153
Unearned Premiums	54,354
Reinsurance Payable	11,944
Amounts Withheld for the Account of Others	1,179
Payroll Taxes Payable (Employer's Portion)	754
Other Liabilities:	
Expense Related:	
Accounts Payable	1,675
Nonexpense Related:	
Premiums Received in Advance	6,664
TOTAL LIABILITIES	91,305
Policyholders' Surplus	1,224,476
TOTAL	$1,315,781

Spring Grove Mutual Insurance Company
Statement of Operations
For the Year 2002

Net Premiums and Assessments Earned		$76,507
Deduct:		
Net Losses Incurred	$94,111	
Net Loss Adjustment Expenses Incurred	12,860	
Other Underwriting Expenses Incurred	76,597	
Total Losses and Expenses Incurred		183,568
Net Underwriting Gain (Loss)		(107,061)
Net Investment Income:		
Net Investment Income Earned	49,849	
Net Realized Capital Gains	490	
Total Investment Income		50,339
Other Income:		
Miscellaneous Income (Expense)	926	
Total Other Income		926
Net Income (Loss) Before Policyholder Dividends and Before Federal Income Taxes		(55,796)
Policyholder Refunds or Dividends		0
Net Income (Loss) Before Federal Income Taxes		(55,796)
Federal Income Taxes Incurred		0
Net Income (Loss)		$(55,796)

Spring Grove Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2002

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2002	**2001**	**2000**	**1999**	**1998**
Surplus, beginning of year	$1,327,543	$1,306,212	$1,268,534	$1,310,464	$1,275,801
Net income	(55,796)	28,826	20,201	(36,733)	18,215
Net unrealized capital gains or (losses)	(48,816	(9,041)	(21,342	(5,197)	16,448
Change in non-admitted assets	1,546	1,546	(3,865)		
Surplus, end year	$1,224,477	$1,327,543	$1,306212	$1,268,534	$1,310,464

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders’ surplus.

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Articles of Incorporation – It is recommended that any changes in the articles of incorporation or bylaws be filed timely, and approved by the Office of the Commissioner of insurance in compliance with s. Ins 612.04, Wis. Stat.

   Action – The company had one change to its articles of incorporation. Filing for the change to the article of incorporation was done on March 23, 2001. The company is in compliance.

2. Invested Asset **–** It is recommended that repurchase agreement be classified as bonds in future statutory annual statements.

   Action – The company is in compliance.

3. Agents' Balances or Uncollected Premium **–** It is recommended that the company nonadmit premium balances that are 90 days past due in compliance with the annual statement instructions.

   Action – The company is in compliance.

4. Unpaid Losses **–** It is recommended that the company establish reserves for all unpaid losses that occurred prior to the annual statement date.

   Action – The company is in compliance.

5. Premiums Paid in Advance **–** It is recommended that the company research, and correct the programming errors in its EDP system, to ensure that premium accounting data files and reports reflect the correct transactions and correct premium balances.

   Action – The company has plans to replace its current software in July 2003 and it is expected to correct the noted problems.

6. Real Estate **–** It is recommended that in the future the company obtain prior approval from the Office of the Commissioner of Insurance before purchasing real estate in compliance with s. Ins 6.20 (6) (d) (6), Wis. Adm. Code.

   Action – The company has not purchased any real estate since prior examination.

7. Real Estate **–** It is recommended that the company comply with s. 612.36 (2), Wis. Stat., in the future by limiting its real estate investment to 1 mill on the dollar of insurance in force.

   Action – The company is in compliance.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent period.

The company amended its 2002 Annual Statement to record additional 2002 excess reinsurance recoverable on paid losses of $177,152. Through discussions with company management, the examiners were told that the board had rather lengthy deliberations over whether or not to pursue the noted recoverable. However, a review of the minutes noted no discussion on the Board’s decision to recover the reinsurance recoverable. It is recommended that the company include detailed information on business discussions and decisions regarding significant financial decisions in its board minutes.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employes which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity Blanket Bond	$75,000
Worker's compensation	Statutory
Bodily Injury	
By accident	100,000 each accident
By Disease	500,000 each employe
By Disease	100,000 policy limit
Errors and Omissions	
Agents	1,000,000 each claim and in the aggregate Deductible: 1,500 each
Professional Liability & Directors and Officers	1,000,000 each claim and 2,000,000 in the aggregate Deduction: 5,000 each claim
Business Owner's Policy	
Building	270,000
Contents Special	56,000
Commercial General Liability	1,000,000
Medical expenses	5,000 per person
Fire Legal liability	100,000 any one fire or explosion

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and of renewal business is inspected by committee members independent of the risk under consideration and review.

The examiner reviewed the ten largest risks to apply the provisions of the reinsurance contract where applicable. It was noted that the company does not reconcile changes made by the reinsurer on returned loss bordereau worksheets. Discrepancies were found with ceding percentages. It is recommended that the company prepares reconciliation for the loss bordereau on a monthly basis.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained;
2. A proper cash receipts journal is maintained;
3. A proper cash disbursements journal is maintained;
4. A proper general journal is maintained; and
5. A proper general ledger is maintained.

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2002.

The company is not audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. Access to the computers is limited to people authorized to use the computers.

During the examination it was noted that the company is currently in the process of replacing its software. The company expects to begin using the new software in July, 2003.

Company personnel back up the computers daily to a tape drive and the backed-up data is kept off-site. Month-end and year-end back up is also done and kept in a locked, fire-proof file cabinet.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Disaster Recovery Plan

A disaster recovery plan identifies steps to be performed in case the company loses a key employe; is not able to access its computer; information on its computer was lost; or the office building was destroyed, to name a few contingencies. The company has developed a disaster recovery plan.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employes of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

Section Ins 6.20 (6), Wis. Adm. Code, allows a town mutual to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the company has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$391,305
2.	Liabilities plus 33% of gross premiums written	165,902
3.	Liabilities plus 50% of net premiums written	132,420
4.	Amount required (greater of 1, 2, or 3)	391,305
5.	Amount of Type 1 investments as of 12/31/2002	511,584
6.	Excess or (deficiency)	$120,279

The company has sufficient Type 1 investments.

ASSETS

Cash and Invested Cash **$371,055**

The above asset is comprised of the following types of cash items:

Cash in company's office	$50
Cash deposited in banks-checking accounts	12,987
Cash deposited in banks at interest	358,018
Total	$371,055

Cash in the company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of the checking account balance was made by obtaining confirmations directly from the depository and reconciling the amount shown thereon to company records.

Cash deposited in banks represents the aggregate of eight deposits in seven depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2002 totaled $25,765 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 3.45% to 6.00%. Accrued interest on cash deposits totaled $2,313 at year-end.

Book Value of Bonds **$271,536**

The above asset consists of the aggregate book value of bonds and a repurchase agreement held by the company as of December 31, 2002. Bonds owned by the company and the repurchase agreement are located in a safe deposit box at a local bank.

Bonds and the repurchase agreement were physically inspected by the examiner. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2002 on bonds amounted to $19,020 and was traced to cash receipts records. Accrued interest of $2,217 at December 31, 2002, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$379,443**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2002. Stocks owned by the company are located in a safe deposit box at a local bank.

Stock certificates were physically examined by the examiner. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2002 on stocks and mutual funds amounted to $11,459 and were traced to cash receipts records. There were no accrued dividends at December 31, 2002.

Book Value of Real Estate **$76,051**

The above amount represents the company's investment in real estate as of December 31, 2002. The company's real estate holdings consist of land, buildings and improvements.

The required documents supporting the validity of this investment were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Premiums and Agent's Balances in Course of Collection **$1,802**

The above ledger asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts verified the accuracy of this asset.

Premiums, Agents' Balances, and Installments Booked but Deferred **$15,144**

The above ledger asset represents premiums and agents' balances receivable, but not yet due because of the billing mode.

This asset was documented by an automated report which itemizes the company's calculation of installments booked but deferred and not yet due for each policy in force as of December 31, 2002. The examiners' review of this report, including recalculation of the company's results for policies selected on a sample basis, verified the accuracy of the asset.

Investment Income Due and Accrued **$4,530**

Interest due and accrued on the various assets of the company at December 31, 2002, consists of the following:

Cash Deposited at Interest	$2,313
Bonds	2,217

The amount was verified by tracing to subsequent cash receipts.

Reinsurance Recoverable on Paid Losses **$189,319**

The above asset represents recoveries due to the company from reinsurance on losses which were paid on or prior to December 31, 2002. A review of year-end accountings with the reinsurer verified the above asset.

Electronic Data Processing Equipment **$6,901**

This asset consists of computer equipment and printer owned by the company at December 31, 2002. A review of the equipment inventory and depreciation schedule verified this asset.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$12,387**

This liability represents losses incurred on or prior to December 31, 2002, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	**Examiners' Development**	**Difference**
Incurred But Unpaid Losses	$23,513	$12,702	$10,811
Less:			
Reinsurance Recoverable on Unpaid Losses	11,121	4,676	6,445
Net Unpaid Losses	$12,392	$8,026	$4,366

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2002. To the actual paid loss figures was added an estimated amount for those 2002 and prior losses remaining unpaid at the examination date.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained;
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates; and
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **$500**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2002, but remained unpaid as of year-end. The methodology used by the company in establishing this liability is the inventory method plus a provision for incurred but not reported claims based on prior years' experience.

The examiners' analysis of expenses incurred in the current year related to the settlements of the prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Unearned Premiums **$54,354**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology.

Reinsurance Payable **$11,944**

This liability consists of amounts due to the company's reinsurer at December 31, 2002, relating to transactions which occurred on or prior to that date. Subsequent cash disbursements and reinsurance accountings verified the reasonableness of this liability.

Fire Department Dues Payable **$153**

This liability represents the fire department dues payable at December 31, 2002. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Commissions Payable **$1,695**

This liability consists of commissions due to the agents at year-end 2002. The examiners reviewed the company’s commission statement and found this liability to be correctly calculated. Supporting records and subsequent cash disbursements verified this item.

Amounts Withheld for the Account of Others **$1,179**

This liability represents employe payroll deductions in the possession of the company at December 31, 2002. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$754**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2002, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Premiums Received in Advance **$6,664**

This liability represents premium paid in advance as of December 31, 2002. Prior recommendations noted that the premium paid in advance report produced by the company's EDP system contains some data errors. The report reflects total annual premium amounts for policies rather than actual cash amounts paid in advance which overstated the balance. The current examination noted that a premium receipt for a policy effective in the subsequent year was not included in the advance premium report which resulted in an immaterial understatement of this balance. The overall review of this balance notes that the balance appears adequately stated. In addition, the company has plans to replace its current software in July 2003 and is expected to correct the noted problems.

Accounts Payable **$1,675**

This liability consists of wages, personal property taxes, and other general expenses the company incurred prior to December 31, 2002 which had not yet been paid. The amount was determined by the examiner by reviewing invoices, cash disbursements, and other supporting records.

The examiner searched for unrecorded liabilities and noted that wages and salaries were not accrued at year end. In addition, the company did not include a payment for service incurred in December 2002. No examination adjustment is necessary as the amount is below the examination tolerable error. It is recommended that expense related liabilities for unpaid obligations, including accounts payable and accrued salaries and wages, be included in the annual statement in accordance with the Town Mutual Annual Statement.

V. CONCLUSION

The examiner's review of the company's accounts did not result in any reclassification of account balances or adjustments to surplus.

The prior examination resulted in seven recommendations. The company complied with all seven recommendations. The current examination resulted in three recommendations, which pertain to corporate records, underwriting and accounts payable.

Surplus has decreased 6% from 1998 primarily due to the unfavorable loss experiences in 2002, including four major house fires and one barn fire. The company has experienced a fluctuating loss ratio, but the expense ratio remains relatively high primarily due to its small premium volume. Despite the poor results in terms of the expenses, and to a lesser extent losses, the company continues to have adequate surplus due to its low premium to surplus ratio.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 14 - Corporate Records—It is recommended that the company include detailed information on business discussions and decisions regarding significant financial decisions in its board minutes.

2. Page 15 - Underwriting—It is recommended that the company prepares reconciliation for the loss bordereau on a monthly basis.

3. Page 24 - Account Payable—It is recommended that expense related liabilities for unpaid obligations, including accounts payable and accrued salaries and wages, be included in the annual statement in accordance with the Town Mutual Annual Statement.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Jean Suchomel of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Respectfully submitted,

Sheur Yang
Examiner-in-Charge